

**Office of Chief Counsel
Internal Revenue Service
Memorandum**

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date: March 24, 2009

to:

General Attorney
(Tax Exempt & Government Entities)

from:

Senior Technician Reviewer
(Procedure & Administration, Branch 2)

subject: Assessing Employee Share of FICA in SECA Tax Court Proceeding

This Chief Counsel Advice responds to your request for assistance dated March 3, 2009. TEGE asked whether section 6521, a limited mitigation provision, allows the Internal Revenue Service (Service) to assess unpaid Federal Insurance Contribution Act (FICA) taxes during the pendency of a Tax Court proceeding arising from the issuance of a statutory notice of deficiency for Self-Employment Compensation Act (SECA) taxes when the assessment statute of limitations for the FICA taxes has expired. This advice may not be used or cited as precedent.

ISSUES

1. Whether the Service may use the mitigation provision of section 6521 to assess FICA taxes against a taxpayer when the taxpayer has not paid FICA taxes or remitted SECA taxes and the statute of limitations under section 6501 has expired with respect to the taxpayer's share of FICA taxes?
2. If section 6521 applies, can the Service assess the FICA taxes during the pendency of the Tax Court case?
3. If a reduction or offset is permitted under section 6521, should the reduction or offset be included below the line in a decision document?

CONCLUSIONS

1. Section 6521 does not provide a mechanism to assess FICA or SECA taxes. Instead, section 6521 operates to mitigate the expiration of the statute of limitations on assessment of FICA (or SECA) taxes when a taxpayer's employment status is erroneously classified and either self-employment income is incorrectly classified as wages and FICA taxes are paid, or wages are incorrectly classified as self-employment income and self-employment taxes are paid. When applicable, this provision provides a reduction or offset between and based upon the tax erroneously paid and the tax actually due. Under the circumstances described below, no reduction or offset is available under section 6521.
2. Section 6521 does not apply to the facts discussed below and, therefore, no assessment of FICA taxes is permitted during the pendency of the Tax Court case or otherwise.
3. Under the facts presented below, a reduction or offset is not permitted by section 6521.

FACTS

Your request for advice and subsequent telephone call provided the following facts. Taxpayers treated as independent contractors and not as employees receive Form 1099s reporting remuneration earned by the taxpayers in each calendar year. Some of these taxpayers report the amount listed in Box 7 of Form 1099, non-employee compensation, as wages from employment on their Form 1040s without paying the employee share of FICA taxes attributable to those wages. These taxpayers, therefore, have not paid either their share of FICA taxes under section 3101 or SECA taxes under section 1401 on these earnings.

Upon receipt of the Form 1040s, the Service identifies the disparity of Form 1099 non-employee compensation reported as wages and, pursuant to an SBSE initiative, automatically issues statutory notices of deficiency to the taxpayers asserting that the amounts reported as wages from employment on the Form 1040s should have been reported as self-employment income and that the taxpayers are liable for unpaid SECA taxes. At the time these statutory notices of deficiency are issued, however, the Service has not yet performed an examination to determine the proper worker classification of the taxpayers.

A number of these taxpayers petition the Tax Court arguing that they are employees, not self-employed individuals, and are thus subject to FICA taxes, not SECA taxes. These cases often involve facts indicating that the taxpayer is an employee. Often, and

for purposes of this advice, the statute of limitations on assessment under section 6501 has run with respect to the employee share of FICA taxes.

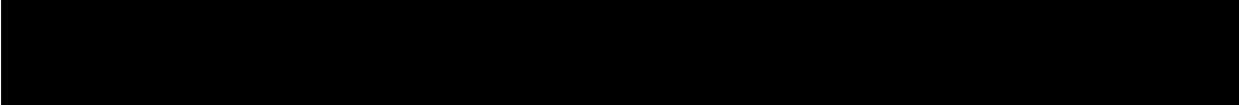
LAW AND ANALYSIS

Employees, as defined in section 3121(d), receive Form W-2s reporting, among other items, wages from employment and the amount of social security and Medicare taxes (FICA taxes) withheld during the year. Non-employees receive Form 1099-MISCs reporting non-employee compensation, among other items.

Section 3101 imposes the employee's share of FICA taxes equal to 7.65% of wages. Section 3102 requires an employer to withhold an employee's FICA taxes from the employee's wages at the time of payment and remit the amounts to the government. Treas. Reg. §31.6011(a)-1(a) requires that an employer make a quarterly return on Form 941 for each calendar quarter in which it pays wages that are subject to FICA taxes. The Form 941 is the required tax return for reporting both the employee's and employer's share of FICA.

Self-employed individuals are not subject to FICA taxes, but are instead subject to SECA taxes imposed by section 1401. This section imposes a tax on self-employed individuals equal to 15.3% of self-employment income. Individuals with self-employment income over the applicable threshold amount are required to report the income on their Form 1040 and remit SECA taxes. Treas. Reg. §1.6017-1(a)(2).

As the facts indicate, the assessment statute of limitations has run with respect to the FICA taxes due and unpaid in some of the cases before the Tax Court. 

 It is not until a later time, typically when the taxpayer petitions the Tax Court, that this issue arises.

Section 6521 can, in certain circumstances, mitigate the effects of an expired period of limitations in the case of FICA and SECA taxes. Section 6521 does not provide a mechanism to assess FICA or SECA taxes but instead provides limited mitigation of the expiration of the assessment statute of limitations for FICA or SECA taxes when a taxpayer's employment status is erroneously classified and either self-employment income is incorrectly classified as wages and FICA taxes are paid, or wages are incorrectly classified as self-employment income and self-employment taxes are paid. Section 6521 mitigates these types of errors by providing a reduction or offset of the amount erroneously paid by the amount actually due, or of the amount actually due by the amount erroneously paid, despite the expiration of the limitations period as to one of the taxes.

Section 6521 will mitigate the effects of an expired period of limitations when:

- (a) An amount is erroneously treated as self-employment income or an amount is erroneously treated as wages;
- (b) Correction of the error requires the assessment of one tax and the refund or credit of another; and
- (c) Correction of one tax is authorized, but the other tax is prevented by any rule of law (other than section 7122).

If the three requirements of section 6521(a) are satisfied, when the authorized correction is made the amount of the allowable assessment or refund will be reduced by the refund or assessment that would be required if such was not prevented by law. This reduction will only occur, however, if the three requirements of section 6521 have been satisfied, (i.e., erroneous treatment of compensation, assessment of the unpaid tax and refund/credit of the paid tax, and correction is possible as to one but not both taxes).

The legislative history of section 6521 and Treas. Reg. §301.6521-1 provide several examples of the operation of section 6521. For instance, Treas. Reg. §301.6521-1(f) reads:

Another illustration of the operation of section 6521 is the case of a taxpayer who, for 1955, is erroneously taxed on \$2,500 as wages, the tax on which is \$50, and who reports no self-employment income. After the period of limitations has run on the refund of the tax under the Federal Insurance Contributions Act, it is determined that the amount treated as wages should have been reported as net earnings from self-employment. The taxpayer's self-employment income would then be \$2,500 and the tax thereon would be \$75. Assume that the period of limitations applicable to subtitle A of the Code has not expired, and that a notice of deficiency may properly be issued. Under section 6521, the amount of the deficiency of \$75 must be reduced by the barred overpayment of \$50.

All of the examples contained in the section 6521 legislative history and regulations present situations where either FICA taxes or SECA taxes were paid by the taxpayer or on the taxpayers' behalf (i.e., the taxpayer has satisfied condition (b)). Under the facts presented above, however, conditions (a) and (c) are satisfied, but condition (b) is not satisfied. Condition (b) is not satisfied because neither the employers withheld, nor the taxpayers paid, the FICA taxes due with respect to the wages earned by the taxpayers, and no SECA taxes were paid by the taxpayers. Therefore, section 6521 is not available to mitigate the effects of an expired assessment limitations period under the factual circumstances described above.

In cases currently before the Tax Court where the Service will concede the taxpayer's status as an employee, assessment of the unpaid FICA taxes is foreclosed by section

6501, and neither FICA nor SECA taxes have been paid, section 6521 cannot be utilized for mitigation purposes. The result is the same in cases not currently before the Tax Court where the statute of limitations under section 6501 has run with respect to FICA taxes and neither FICA nor SECA taxes were paid. In these situations the taxpayers must enter into closing agreements with the Service, agreeing to the amount and assessment of the FICA tax liability, in order for the Service to collect these taxes.

[REDACTED]

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This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call Procedure and Administration, Branch 2 at (202) 622-4940 if you have any further questions.